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INVESTMENT MANAGEMENT

As We See It

> History teaches us that men and nations behave wisely once they have exhausted all other alternatives.
>
> --Unknown

One investment theme we have pursued places an emphasis on identifying U.S. companies which can benefit from the rapid growth expected in developing countries, e.g., China, India, and Mexico. As we pursue this approach we are reminded of the disparate level of economic development between countries historically. While the West (Western Europe, the United States, Canada, Australia, Japan,and a few others) enjoys prosperity, many regions of the world remain impoverished. Why has economic growth of countries been so uneven for so long?

Historians have given many reasons for the Western world's economic miracle. Everything from science and invention, natural resources, exploitation of workers, colonialism and imperialism, and slavery have been used to explain the West's rise from poverty to wealth. These and other popular explanations for the economic gap between the West and the rest of the world are refuted in *How The West Grew Rich* by Nathan Rosenberg and L. E. Birdzell, Jr.. They conclude Western societies benefited from a relaxation in political and religious restrictions. Unconstrained, their citizens were allowed to experiment and innovate. More importantly, they were afforded the benefits arising from their experimentation and innovation, as well as, the adverse consequences of their misjudgments.

The authors believe, "The West's sustained economic growth began with the emergence of an economic sphere with a high degree of autonomy from political and religious control." Relaxation from political control began in the Middle Ages and took several forms. For example, trade was increasingly allowed at unregulated prices. Prior to that time, prices were pre-determined by political authorities. Additionally, the guilds and governments gradually lost control over the entrepreneurial process. In terms of modern economics, there was a gradual repeal of price controls and a movement toward deregulation.

Autonomy of business affairs from religious control came in the sixteenth and seventeenth centuries. As business ". . . grew increasingly independent of ecclesiastic authority, it acquired a much higher degree of autonomy . . . than it had previously possessed. Religion was gradually transformed from a restraining influence upon capitalist development to a force that both sanctioned and supported mercantile capitalism by precisely the moral teachings required for the smooth running of the rising commercial system."

Innovation and experimentation fostered the spread of mercantilism, as merchants increasingly succeeded in escaping political and religious control. This promoted the financing of trading voyages over long distances, encouraged the establishment of large shops outside guild jurisdictions, inspired the introduction of new and improved products, and eventually the development of new forms of business organizations. Innovation and experimentation, however, meant uncertainty and unpredictability and produced severe penalties for failure. Yet, the West, with ample rewards for success was able to encourage innovation and experimentation which over time did lead to economic advancement.

In summary, Rosenberg and Birdzell state, "Initially, the West's achievement of autonomy stemmed from a relaxation, or a weakening, of political and religious controls, giving other departments of social life the opportunity to experiment with change. . . . And successful change requires a large measure of freedom to experiment. A grant of that kind of freedom costs a society's rulers their feeling of control, as if they are conceding to others the power to determine the society's future. The great majority of societies, past and present, have not allowed it. Nor have they escaped from poverty."

Awareness of the reasons for a society's long-term economic success can be quite useful to investors. Such knowledge helps to explain what economic, political, and social policies are likely to lead to the continuance of Western economic growth, what policies are likely to help less-developed countries grow, and what policies might lead to a society's decline. It is from this comprehensive perspective that we analyze the economic potential of foreign operations of U.S. Companies.

We have chosen not to invest directly in the securities of foreign corporations, but rather we seek to identify the U.S. corporations which may benefit from foreign economic growth. Toward that end we are emphasizing U.S. companies which are investing in those countries which exhibit economic characteristics consistent with those qualities which have led to success in the past.

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